

Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-08 FRB-03
INR-07 NSAE-00 USIA-06 TRSE-00 XMB-02 OPIC-03
SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-06
CEA-01 PA-01 PRS-01 /084 W
-----121809 241858Z /66

R 241701Z JAN 78 ZDS
FM AMEMBASSY BONN
TO SECSTATE WASHDC 5137
DEPARTMENT TREASURY
INFO AMCONSUL DUSSELDORF

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E.O. 11652: N/A
TAGS: EFIN, GW
SUBJECT: ESSEN INSTITUTE ON FRG ECONOMIC PERFORMANCE

REF: BONN (77) 19869

1. SUMMARY --ESSEN INSTITUTE TAKES DIM VIEW OF GERMAN
ECONOMIC PROSPECTS; BLAMES UNCERTAINTY ARISING OUT OF

INFLATIONARY WAGE INCREASES AND THE SHIFTING DIRECTION
OF MACROECONOMIC POLICIES FOR THE ON-AGAIN/OFF-AGAIN FRG
ECONOMIC PERFORMANCE OF RECENT YEARS. END SUMMARY.

2. EMBOFF MET WITH STAFF MEMBERS RHINE-WESTPHALIA
INSTITUTE FOR ECONOMIC RESEARCH ESSEN ON
JANUARY 20 TO DISCUSS OUTLOOK FOR GERMAN ECONOMY. WITH
60 PROFESSIONALS, ESSEN INSTITUTE IS ONE OF THE SMALLER
OF THE FIVE FRG INSTITUTES ENGAGED IN ECONOMIC AND
BUSINESS RESEARCH. LIKE THE OTHERS, IT IS AN INDEPENDENT
CORPORATION WHOSE INCOME IS DERIVED FROM FEDERAL AND
STATE SUBSIDIES, CONTRIBUTIONS, AND RESEARCH AND STUDIES
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FOR PRIVATE AND PUBLIC ENTITIES. PREVIOUSLY LESS WELL
REGARDED THAN SOME OF ITS RIVALS, THE ESSEN INSTITUTE
RECENTLY GAINED IN RELATIVE PUBLIC ESTEEM BY ITS BETTER
ESTIMATE OF 1977 GNP GROWTH THAN THE OTHER INSTITUTES
WHICH WERE FAR TOO OPTIMISTIC. LESS WELL KNOWN,
ACCORDING TO OUR ECONOMICS MINISTRY CONTACTS, IS THE
FACT THAT THEY WERE RIGHT FOR THE WRONG REASONS --

OFFSETTING ERRORS IN THE BADLY ESTIMATED COMPONENTS OF GNP.

3. THE ESSEN INSTITUTE, CLASSICAL MONETARIST IN ITS PHILOSOPHICAL ORIENTATION, IS SKEPTICAL THAT THE FRG'S TAX/EXPENDITURE PROGRAMS WILL HAVE MUCH REJUVENATING IMPACT ON THE ECONOMY IN 1978 AND ARE INDEED CONVINCED

THAT THE EFFECTS OF EVER CHANGING TAX RATES AND PUBLIC SECTOR DEMAND ARE PERNICIOUS IN THE LONG RUN.

4. WHAT LITTLE ADDITIONAL STIMULATION THE ECONOMY MAY RECEIVE IN 1978 THE ESSEN INSTITUTE EXPECTS TO COME FROM INVESTMENT -- PARTLY FROM THE PUBLIC AND PARTLY FROM THE PRIVATE SECTORS. WITH SOMEWHAT LOWER WAGE SETTLEMENTS EXPECTED IN 1978 (THEY PREDICT AN AVERAGE INCREASE OF 5 PERCENT AS OPPOSED TO 6.5 - 7 PERCENT IN 1977) PROFIT EXPECTATIONS WILL BE IMPROVED (BUT NOT BY NEARLY SO MUCH AS THE 15 PERCENT ESTIMATE OF THE ECONOMICS MINISTRY). THEY EXPECT FALLING EXPORT AND CONSUMPTION GROWTH RATES TO PRETTY MUCH OFFSET THE UPLIFT FROM A HIGHER RATE OF INVESTMENT. RESULT: ANOTHER YEAR OF STAGFLATION, WITH A LITTLE LESS INFLATION. GNP IN THIS PROGNOSIS EXPANDS BY ONLY LIMITED OFFICIAL USE

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2.6 - 2.7 PERCENT.

5. ESSEN'S PRESCRIPTION IS WAGE SETTLEMENTS IN LINE WITH PRODUCTIVITY INCREASES -- ABOUT 2 1/2 PERCENT IN 1978. IN THEIR VIEW, STABLE WAGES WOULD QUICKLY BE

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TRANSLATED INTO STABLE PRICES. THAT HALF OF THE
POPULATION DERIVING ITS BASIC INCOME FROM PROPERTY,
PENSIONS AND ENTREPRENEURSHIP WOULD IMMEDIATELY
EXPERIENCE A POSITIVE REAL INCOME EFFECT AND SHORTLY
THEREAFTER WAGE EARNERS WOULD ALSO GAIN AS PRICES
STABILIZED WHILE NOMINAL WAGES ADVANCED. THIS
CORRESPONDS CLOSELY WITH THE MESSAGE WHICH THE COUNCIL
OF ECONOMIC EXPERTS GAVE THE FRG IN NOVEMBER (REFTEL).

6. ACCORDING TO ESSEN, THE FLY IN THE OINTMENT IS THE
EXISTENCE OF POWERFUL LABOR UNIONS WHICH PUSH UP WAGES
EXCESSIVELY AND OF A GOVERNMENT WHICH TRIES TO
ACCOMMODATE CONSEQUENT DISEQUILIBRATED MARKETS THROUGH
MONETARY AND FISCAL EXPANSION. STEADY WAGE EXPANSION,
AS OPPOSED TO WIDELY FLUCTUATING WAGE MOVEMENTS
CHARACTERISTIC OF INFLATIONARY SITUATIONS, WOULD
STABILIZE CONSUMPTION PATTERNS AND REDUCE THE
PROPENSITY TO OVERSAVE SUCH AS CURRENTLY IN THE FRG.

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7. AS WAS TO BE EXPECTED, ESSEN INSTITUTE DOES NOT SEE
MUCH THE FRG CAN DO TO HELP THE INTERNATIONAL ECONOMY,
EXCEPT TO SET A BETTER EXAMPLE. LIKE SO MANY OTHER
GERMAN OPINION MAKERS, ESSEN HOLDS STRONGLY TO THE VIEW
THAT U.S. BOP PROBLEMS ARE OF ITS OWN MAKING --
PARTICULARLY THE UNECONOMIC PRICING OF ENERGY RESOURCES.
WHILE THE FRG CANNOT ISOLATE ITSELF FROM EXTERNAL WORLD
DISTURBANCES, IT CAN INSULATE ITSELF, SO THEY THINK, BY
KEEPING ITS OWN HOUSE IN ORDER.

8. COMMENT -- ALTHOUGH SHADED RATHER MORE CONSERVA-
TIVELY IN ESSEN THAN IN MOST OTHER CIRCLES, THE VIEW
THAT THE FRG IS DOING ALL IT CAN (AND PERHAPS RATHER MORE
THAN IT OUGHT) FOR ECONOMIC GROWTH IS SHARED WIDELY

AMONG POLITICAL LEADERS, BUSINESS COMMUNITY, ACADEMIA
AND PROBABLY THE COMMUNITY AT LARGE. AGAINST SO MUCH
STOLIDITY OF CONVICTION IT IS DIFFICULT FOR DEMANDS
FROM ABROAD FOR CHANGE MAKE MUCH OF A DENT.
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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 jan 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC CONDITIONS, REPORTS
Control Number: n/a
Copy: SINGLE
Draft Date: 24 jan 1978
Decaption Date: 01 jan 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 20 Mar 2014
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1978BONN01367
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Expiration:
Film Number: D780036-0050
Format: TEL
From: BONN
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1978/newtext/t19780131/aaaaazrj.tel
Line Count: 175
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: cbef24e1-c288-dd11-92da-001cc4696bcc
Office: ACTION EUR
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: n/a
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 05 may 2005
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: N/A
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 3727484
Secure: OPEN
Status: NATIVE
Subject: ESSEN INSTITUTE ON FRG ECONOMIC PERFORMANCE
TAGS: EFIN, GE, ESSEN INSTITUTE
To: STATE TRSY
Type: TE
vdkgvwkey: odb://SAS/SAS.dbo.SAS_Docs/cbef24e1-c288-dd11-92da-001cc4696bcc
Review Markings:
Sheryl P. Walter
Declassified/Released
US Department of State
EO Systematic Review
20 Mar 2014
Markings: Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014